

AUTOPSY OF MUNICIPAL FAILURE: THE CASE OF CENTRAL DARLING SHIRE

Joseph Drew

Research Fellow, Institute for Public Policy and Governance, University of Technology Sydney, NSW, 2007, Australia. Email: Joseph.Drew@uts.edu.au

Nicole Campbell

Project Manager, Institute for Public Policy and Governance, University of Technology Sydney, NSW, 2007 Australia. Email: Nicole.Campbell@uts.edu.au

ABSTRACT: Local government plays a vital role in providing infrastructure, services and employment to rural and regional communities. Indeed, threats to the fiscal viability of regional councils may well jeopardise the sustainability of an entire community. In December 2013 the New South Wales (NSW) Minister for Local Government suspended Central Darling Shire (in far-western NSW) and appointed an interim Administrator in response to an unprecedented liquidity crisis. In October 2014 a public inquiry recommended extension of the period of administration until September 2020. This paper considers the processes leading up to this extraordinarily lengthy period of financial administration. In particular, we examine the claim that an inequitable allocation of Financial Assistance Grants (FAGs) was a major factor in bringing about the Shire's liquidity crisis. We conclude our analysis with some recommendations for changes to FAG allocations which will help ensure sustainable futures for rural communities.

KEY WORDS: Central Darling Shire; Financial Assistance Grants (FAGs); local government failure; state government oversight.

1. INTRODUCTION

Central Darling Shire is located 970 km from Sydney in far Western NSW. The Shire covers 5 349 380 hectares, which is about 60 per cent of the size of Tasmania or over one-fifth of the size of the entire United Kingdom (Australian Bureau of Statistics (ABS), 2014). The municipality is responsible for a range of government functions, inclusive of the maintenance of 1 602 km of road infrastructure, and four aerodromes which are used by the Royal Flying Doctor Service, State Emergency Service and Rural Fire Service (Office of Local Government (OLG), 2015). Yet Central Darling has a comparatively small rating base of just 1 580 properties (1 078 residential, 362 farm and 140 businesses) clustered around four small towns which are separated by vast distances

(the distances relative to the council chambers in Wilcannia are: Menindee 306 km, White Cliffs 94 km and Ivanhoe 182 km) This disparity between infrastructure responsibilities and taxation base is exacerbated by harsh constraints of circumstance: Central Darling has the second lowest socio-economic rating in the state; Indigeneity of 38.3 per cent and an unemployment rate of 13.1 per cent. In addition, market failure owing to remote location and low population density means that Council is often called upon to provide important, one-off 'placed based' commercial services to the community (see, for example, Dollery *et al.*, 2010). In remote regions with a small and declining population base many services simply aren't a commercially viable proposition. Local governments are then often faced with a stark choice: accept that communities will no longer have access to essential services such as banking and postal facilities, or, intervene and take over the running of the service at a financial loss. Examples of Central Darling Shire interventions to address market failure include the operation of the Wilcannia Post Office (since the previous owners fell into receivership); the operation of the Westpac banking agency and the operation of two caravan parks to accommodate tourists.

The combination of environmental constraints, a heavy infrastructure burden and low taxation base has resulted in the Shire experiencing acute fiscal distress over a number of years. From at least January 2011 various official reports cast doubt on the council's long-term sustainability. On 23 December 2013 the (then) NSW Minister for Local Government suspended the council and appointed an interim Administrator pursuant to clause 413E of the Local Government (General) Regulation 2005, in response to an unprecedented 'real possibility of the Council running out of cash in the next few months' (OLG, 2014, p. 5). This interim order was extended for an additional three months in March 2014. In October 2014 the Minister for Local Government (Paul Toole) commissioned a Public Inquiry which led to Civic Offices being declared vacant until September 2020.

In a stinging assessment of Councillor's performances the state government's suspension report assessment says (*sic*) that "most – if not all – of the maladies affecting the Council may be laid squarely at the feet of a lack of leadership and managerial expertise at both the elected and staff levels of the organisation" (Bajkowski, 2014). However, from the outset the mayor and councillors of Central Darling sought to highlight the role of insufficient intergovernmental grants in the Shire's liquidity crisis. Moreover, elected representatives made considerable efforts at the Public Inquiry to emphasise what they felt to be inequitable

intergovernmental grant allocations. In the *Central Darling Shire Council Public Inquiry Report*, Commissioner Colley was critical of councillor reticence to accept responsibility for the fiscal plight of the Shire and noted his 'great concern [that], instead of considering remedial budgetary actions, there has been a propensity to blame others for the situation' (Colley, 2014, p. 60).

Since 1973 the federal government has provided intergovernmental grants to councils with the objective of achieving horizontal fiscal equalisation (HFE). HFE seeks to provide councils with the capacity 'to provide their residents with an equitable level of services' (Local Government (Financial Assistance) Act 1995, s3(2)(b)). The need for HFE arises as a result of: (i) vertical fiscal imbalance whereby the federal government has powers to collect the bulk of taxation and (ii) horizontal fiscal imbalance arising from different revenue raising capacities and expenditure attributes of Australian municipalities (Drew and Dollery, 2015a). Due to the absence of constitutional recognition for Australian local government, the federal HFE grants are allocated by seven separate Grants Commissions operated by the states and the Northern Territory (Drew and Dollery, 2015a). Notably, the Commissioner of the Public Inquiry into the Central Darling Shire liquidity crisis was also the Chair of the NSW Local Government Grants Commission (NSWLGGC, 2014).

Our central concerns in this context are to undertake a critical investigation into the process of placing Central Darling Shire into Administration for such an extended period, and to query the public reasons for so doing against the backdrop of Australia's fiscal federalism generally and the regime of transfers designed to accomplish HFE in particular. The paper itself is divided into six main parts. Following this introductory section, Section 2 provides a brief overview of the operational context of the Central Darling Shire including a comparative summary of environmental constraints, revenue metrics and functional expenditure with respect to the other twenty councils occupying the same OLG classification. Section 3 provides a review of the theory and literature on intergovernmental grants. Section 4 outlines important events leading up to the decision to appoint a permanent Administrator. We then provide a summary in Section 5 of the Public Inquiry, with particular reference to the matter of intergovernmental grant allocations. The paper ends in Section 6 with a number of recommendations relating to the equitable distribution of HFE grants and observations on the procedural fairness of the Inquiry.

2. CENTRAL DARLING SHIRE OPERATIONAL CONTEXT

Table 1 provides details of the environmental constraints facing Central Darling Shire, along with comparative data for the other twenty councils classified as Group 9 municipalities (medium size, remote and agricultural councils). Notably Central Darling has the lowest socio-economic rating in the cohort (the second lowest in the state), the lowest population density, highest proportion of Aboriginal and Torres Strait Islander (ATSI) individuals in the cohort (and second highest in the state), the second highest unemployment rate in the cohort (fourth highest in the state) and highest metre road length per capita for the state (OLG, 2015). The environmental constraint data is brought into stark relief by the arithmetic mean of the various metrics for the state, presented in the last row of Table 1. In sum, it is clear that the residents of Central Darling have arguably the highest need for municipal goods and services in the state whilst also exhibiting one of the lowest capacities to pay for them. This environmental constraint data suggests that the Shire might require comparatively high levels of HFE grant aide.

Table 2 details the Financial Assistance Grants allocations for Group 9 councils in the 2012/13 financial year (the year upon which the Commissioner would have based his recommendations). FAG grants are allocated in two tranches – General Purpose grants and Road grants – even though both allocations are untied. Central Darling Shire received the highest General Purpose allocation in the cohort; however, the quantum of the grant was just two-thirds of the NSW average. On a per assessment basis, the Shire received the highest General Purpose allocation in the state. However, it is important to be mindful of the stated purpose of HFE grants – ‘to allow councils to function at a standard not lower than the average standard in the State’ – when assessing whether the Shire’s quantum was sufficient (Local Government (Financial Assistance) Act, 1995). The final column of Table 2 details the quantum of road allocation, which we also present in per kilometre terms in parentheses. Central Darling received the fourth highest quantum in the cohort, but curiously received a lower quantum than Lockhart council, which maintains 114 km less road distance. Moreover, on a per kilometre basis the Shire received the lowest road allocation in the cohort and an allocation which was almost half of the state mean. This anomaly results from the NSW Local Government Grants Commission’s use of population data as a key input into the road grant allocation algorithm (see Drew and Dollery, 2015a).

Table 1. Environmental Constraints of Medium Remote and Agricultural Category Municipalities, 2013.

Council	Socio Economic Rating	Population Density (capita/km²)	Length of Roads (km)	ATSI (%)	Un-employment Rate (%)	Average Taxable Income (\$)	No. Businesses
Balranald	33	0.1	1328	6.8	4.5	32 816	171
Bogan	40	0.2	1352	14.4	5.8	36 149	188
Bombala	45	0.6	629	2	6.1	36 168	157
Boorowa	74	1	608	2	5.2	35 527	69
Bourke	37	0.1	1883	30.2	14.5	37 544	216
Carrathool	76	0.1	2300	6.6	4	38 064	195
Central Darling	2	0.04	1602	38.3	13.1	38 248	144
Coolamon	80	1.8	1275	2.6	3.9	35 448	232
Coonamble	6	0.4	1393	29.3	8.9	35 735	206
Gilgandra	16	0.9	1293	12.2	6.6	35 615	208
Gundagai	64	1.5	694	2.5	5.1	36 777	167
Guyra	27	1.1	842	10	5.9	32 075	144
Harden	35	2	768	4.5	5.4	35 333	228
Hay	21	0.3	777	5.5	6.8	32 664	211
Lockhart	102	1	1488	2.5	3.7	36 245	251
Murrumbidgee	25	0.7	590	10.2	4	38 150	93
Tumbarumba	59	0.8	465	2.4	4.4	36 278	186
Wakool	82	0.5	1281	2.5	6.1	32 444	270
Walcha	84	0.5	807	7.4	5.2	31 741	156
Warren	49	0.3	964	13.3	6.1	35 985	127
Weddin	52	1.1	968	1.8	5.7	30 621	131
Group Mean	48	0.72	1109.9	9.86	6.24	35 220	179
State Mean	76	780.9	945.36	5.3	6.1	42 912	1 251

Source: Office of Local government (2015); ABS (2015).

Table 2. Financial Assistance Grant Allocations, 2013.

Council	Total No. Assess	Population	General Purpose (\$ per assessment in parentheses)	Road Grants (\$ per km in parentheses)
Balranald	1516	2 371	1 571 497 (974.87)	1 172 720 (883.07)
Bogan	1938	3 037	1 623 020 (840.07)	1 302 018 (963.03)
Bombala	1899	2 401	1 061 603 (561.40)	641 167 (1,019.34)
Boorowa	1890	2 558	833 844 (437.25)	607 116 (998.55)
Bourke	1735	2 996	2 189 941 (1257.14)	1 692 856 (899.02)
Carrathool	1954	2 792	2 038 237 (1017.08)	2 046 343 (889.71)
Central Darling	1606	2 070	2 200 748 (1392.88)	1 409 193 (879.65)
Coolamon	2815	4 276	1 717 641 (607.37)	1 155 421 (906.21)
Coonamble	2567	4 279	1 845 983 (712.18)	1 312 827 (942.45)
Gilgandra	2337	4 488	1 538 735 (657.30)	1 190 715 (920.89)
Gundagai	2538	3 747	1 113 438 (438.53)	736 875 (1,061.78)
Guyra	2422	4 645	1 105 992 (455.14)	842 741 (1,000.88)
Harden	2397	3 762	1 321 322 (542.19)	759 361 (988.75)
Hay	1921	2 962	1 675 700 (871.85)	721 019 (927.95)
Lockhart	2540	3 021	1 768 834 (690.68)	1 422 781 (956.17)
Murrumbidgee	1327	2 503	1 046 024 (785.30)	545 073 (923.85)
Tumbarumba	2521	3 521	1 329 417 (529.02)	519 896 (1 118.06)
Wakool	2829	3 979	2 026 066 (714.91)	1 301 468 (1 015.98)
Walcha	1815	3 087	788 347 (441.65)	822 049 (1 018.65)
Warren	1895	2 910	1 270 954 (669.98)	924 165 (958.68)
Weddin	2569	3 711	1 448 232 (562.64)	901 634 (931.44)
Group Mean	2 144	3 291	1 500 742 (721.88)	1 048 926 (962.10)
State Mean	19 741	48 723	3 171 664 (344.46)	1 262 544 (1 647.70)

Source: Office of Local government (2015); ABS (2015); NSW Local Government Grants Commission (2014).

Table 3 summarises taxation, domestic waste charge and water and sewerage charge data for Group 9 councils for 2012/13. Central Darling Shire had the fifth lowest residential rates and the lowest farm and business rates in the cohort. Moreover, the average rates levied in these categories were well below the state mean. However, the data should be interpreted in the context of the tax limitation regime which has operated in NSW for almost four decades (Drew and Dollery, 2015b). In particular it is important to take account of the total imposts placed on residents, as tax limitations do not apply to annual fees and charges. The final column of Table 3 presents the average cumulative charge to residential ratepayers (residential rates plus water, sewerage and domestic waste).

When considered on this basis the Shire has an impost considerably higher than the cohort average. Indeed, the residential revenue effort – which measures total municipal rates and charges as a function of total income accruing to residents (Ladd and Yinger, 1989) - for Central Darling in 2012 was the highest in the state (3.796%) and well over three times the state mean (1.016%). This own-source revenue data is an important consideration, given that HFE grants take into account the revenue effort exerted by the municipality. We now consider the theory and practice of horizontal fiscal equalisation grants.

Table 3. Own-Source Revenue, 2012/13.

Council	Average Residential Rate (\$)	Average Farm Rate (\$)	Average Business Rate (\$)	Typical Water and Sewer Charge (\$)	Average Domestic Waste Charge (\$)	Total Average Residential Charge (\$)
Balranald	221.48	1 751.66	748.54	1 452	202.46	1 876
Bogan	219.85	2 157.74	1 095.74	1 501	344.16	2 065
Bombala	508.60	2 105.18	872.61	1 125	225.34	1 859
Boorowa	445.98	2 196.48	449.28	1 282	101.57	1 829
Bourke	298.08	2 605.33	430.56	1 683	205.42	2 186
Carrathool	387.03	2 856.79	1 010.26	978	194.56	1 559
Central Darling	233.79	991.83	222.22	1 483	275.80	1 992
Coolamon	289.72	1 642.94	280.17	350	202.10	842
Coonamble	295.87	3 954.75	597.09	651	295.19	1 242
Gilgandra	486.34	3 115.91	817.31	1 109	256.45	1 852
Gundagai	268.62	1 898.29	491.02	1 071	268.62	1 609
Guyra	410.36	2 171.39	631.94	1 106	209.95	1 727
Harden	396.34	2 205.22	706.14	1 647	290.11	2 333
Hay	517.53	2 643.22	1 341.23	1 462	182.93	2 163
Lockhart	231.51	1 397.37	334.66	464	258.49	954
Murrumbidgee	199.16	2 963.18	279.57	640	240.95	1 080
Tumbarumba	375.36	1 556.49	682.80	1 152	310.52	1 838
Wakool	486.52	2 899.68	859.26	1 406	196.08	2 089
Walcha	401.33	3 266.84	666.67	845	304.88	1 551
Warren	456.30	4 980.91	1 267.72	1 267	179.39	1 903
Weddin	381.87	1 216.90	786.26	297	180.63	860
Group Mean	358	2 408	694	1 094	235	1 686
State Mean	712	2195	2693	1 129	298	Not applicable*

Note: *Given that only around half of the councils in NSW conduct water and sewerage operations, it is not possible to calculate a comparable statistic for the state. Source: Office of Local government (2015).

3. INTER-GOVERNMENTAL GRANTS

The need for inter-governmental grants results from two factors which are common to most federalist systems of government. First, most federations are characterised by vertical fiscal imbalance owing to the fact that central governments typically have the greatest taxation powers but relatively less service provision responsibilities (Oates, 1999). For instance, in Australia the Commonwealth Government collects over 80 per cent of the nation's total tax take whilst local government collects just 3.4 per cent (ABS, 2015). Yet local government has significant infrastructure responsibilities, including maintenance of around 80 per cent of the national road network as well as the majority of rural and regional airports (Chakrabarti *et al.*, 2002). Second, the constituent entities of most federations are distinguished by pronounced horizontal fiscal imbalance in terms of both revenue-raising capacity and expenditure need (Oates, 1999). Thus, horizontal fiscal equalisation grants are 'a necessary counterpart to decentralisation, offsetting its tendency to create disparities among regions in the ability to provide public goods and services' (Boadway, 2004, p. 212).

There are many reasons for pursuing HFE in a federation. Most importantly, HFE eliminates inefficient migration of capital and labour which might result if municipalities operated in vastly different fiscal environments (Oates, 1999). However, an effective system of HFE also helps to bind a federation together (Boadway and Shah, 2009), removes potential for political conflict between municipalities (Lecours and Beland, 2013), and eliminates wasteful lobbying and opportunities for pork barrelling. Moreover, for rural and remote councils HFE has an important role to play in regional economic development. For instance, where HFE grants facilitate provision and maintenance of sealed road infrastructure, primary producers enjoy cheaper and faster all-weather access to markets along with higher prices for animal stock (which is subsequently subject to less stress in transit).

In Australia HFE grants are administered according to the Local Government (Financial Assistance) Act 1995. The statute stipulates that funds should be allocated on a full horizontal equalisation basis which:

- (a) Ensures that each local governing body in a state is able to function, by reasonable effort, at a standard not lower than the average standard of other local governing bodies in the state; and
- (b) Takes account of differences in the expenditure required to be incurred by local governing bodies in the performance of their functions and in their capacity to raise revenue' (Local Government (Financial Assistance) Act 1995, s6(3)).

Thus FAG grants should by definition provide councils with the *potential* for service equality, given reasonable revenue effort. It is important to note that *actual* service provision may differ from one municipality to another in accordance with the specific preferences of residents. Indeed, the *raison d'être* of federal systems of government is that 'by tailoring outputs of such goods and services to the particular preferences and circumstances of their constituencies, decentralised provision increases economic welfare above that which results from the more uniform levels of such services that are likely under national provision' (Oates, 1999, p. 1121).

The scholarly literature has been sceptical for some time regarding whether the practice of FAG allocations in Australia does in fact accord with the theory of HFE or, indeed, the definitions provided in the enabling legislation (see, for instance, Dollery and Mounter, 2010; Drew and Dollery, 2015a). One reason why practice diverges from the stated purpose of the legislation can be found in s6(2)(b) of the Act, which stipulates a minimum quantum for each council of 'no less than the amount that would be allocated to the body if 30 per cent of the amount to which the State is entitled under that section in respect to the year were allocated among local governing bodies in the state on a per capita basis'. This distortion of HFE objectives is compounded by the fact that initial state and territory allocations are also based on population size rather than need (see, Commonwealth Grants Commission, 2012). The other reason why actual practice does not accord with the principles of HFE relates to the algorithms employed by the various State Local Government Grants Commissions. For instance, the NSW Local Government Grants Commission (NSWLGGC) employs standard expenditure allowances based on the state average cost of providing twenty different functions over a five-year period. Clearly expenditure allowances based on state averages do not respond to s6(3)(b) of the Act – that is, state averages implicitly (and implausibly) assume that all councils in the jurisdiction face similar costs for providing services.

Moreover, the NSWLGGC generates revenue adjusters to control for ‘revenue effort’ in response to s6(3)(a) using a standard tax rate which is calculated as the quotient of the sum of all general rates levied by all councils in NSW with respect to the sum of rateable unimproved property values for the entire state. Clearly this method of adjusting for revenue effort is flawed on at least three counts. First, for almost four decades NSW has operated a tax limitation regime which caps the total tax take of all councils in the state. It is therefore misleading to suggest that an average tax rate in any way reflects the potential revenue which could be exacted by any particular council (Drew and Dollery, 2015b). Second, the method employed entirely neglects annual fees and charges levied by council. It is particularly concerning that only a partial estimate of municipal impost is made given that there is considerable evidence that tax limitations encourage upward pressure on unregulated fees and charges (Blom-Hansen *et al.*, 2014). Third, municipal taxes are paid out of flows of income *not* stocks of wealth – therefore, the NSWLGGC appears to be calculating ‘effort’ on an entirely incorrect premise (revenue effort calculated as total municipal impost divided by total income accruing to entities in the jurisdiction is the appropriate measure – see, for instance, Ladd and Yinger, 1989).

It appears that the NSWLGGC makes some effort to adjust for differences in need through employing a range of disability factors. However, the process is not transparent and the NSWLGGC makes clear that the disability factors are in part a product of ‘weightings [which are] meant to reflect the significance of the measure in terms of the expected additional cost’ (NSWLGGC, 2014, p. 20). Further, the Commission’s report states that ‘the weightings have generally been determined by establishing a factor for the maximum disability based on a *sample* of councils *or through discussion* with appropriate peak organisations’ (emphasis added, NSWLGGC, 2014, p. 20). This is a rather disappointing and chaotic approach to the allocation of HFE grants, especially given that an empirically robust econometric method for calculating grants has been outlined in the scholarly literature for many decades (Ladd and Yinger, 1989)

We now briefly consider some of the key events leading up to the decision to suspend the democratically elected representatives of Darling Shire until September 2020.

4. CHRONOLOGY OF ADMINISTRATION PROCESS

One of the curious aspects of the unprecedented liquidity crisis faced by Central Darling Shire is that it was preceded by at least three years of adverse reports, ineffective interventions and requests from the Shire for financial assistance (OLG, 2014). This section provides a chronology of key events.

January 2011. The ‘Promoting Better Practice Review’ was initiated into Central Darling Shire by the Department of Local Government (now the Office of Local Government) and conducted by Angus Broad (subsequently appointed assistant to Commissioner Colley). This Review ‘contained fifty six recommendations, highlighting significant concerns about the current performance of the Council’ and ‘comment[ing] on the difficulties faced by the Council in the longer term’ (Colley, 2014, p. 3).

September 2012. Six of the nine incumbent Councillors were returned to office following local government elections. The elected representatives had between six and 23 years of experience as councillors (the mayor had served on council for 18 years).

17 December 2012. The Shire’s ‘Auditor’s Report’ for the preceding financial year noted that the Shire’s liquidity position had ‘deteriorated significantly over the last year’ and that ‘this poor cash position will have a major impact in the Council being able to deliver services into the future’ (Colley, 2014, p. 101).

27 February 2013. The Shire requested a \$2 million finance facility at a meeting with the Minister for Local Government, Minister for Western NSW and Member for Murray-Darling (John Williams) to alleviate a cash flow problem which had arisen due to changes in the way Roads and Maritime Services (RMS) paid for work subcontracted to council (Department of Premier and Cabinet, 2014, p. 38).

February 2013. The Office of Local Government expressed concern that ‘Council’s financial position had deteriorated further and was parlous’ (OLG, 2014, p.2). This prompted an on-site review over the period 12th –14th February which concluded that ‘Council’s financial sustainability in the longer term remained questionable, with its cash position weakening significantly in the last year’ (OLG, 2014, p. 3).

14 March 2013. The NSW Treasury Corporation (TCorp, 2013), commissioned by the Department of Local Government to conduct a review of the financial sustainability of each council in NSW, published its *Central Darling Shire Council Financial Assessment, Sustainability and Benchmarking Report*. TCorp’s (2013) review of Central Darling Shire’s sustainability concluded that ‘we consider Council to be in

deteriorating financial position and to be unsustainable’ (TCorp, 2013, p. 33). Moreover, the Report noted that ‘Council will face liquidity pressures and will have limited capacity to service its debt commitments’ (TCorp, 2013, p. 4).

April 2013. The Department of Local Government (DLG) appointed Mr Geoff Wise, former General Manager of Bourke Shire, as mentor to Central Darling Shire.

10 May 2013. The DLG appointed mentor, Mr Geoff Wise, wrote an ‘Urgent Central Darling Report’ to Mr Grahame Gibbs, Deputy Chair of the NSWLGGC, and copied same to Deputy Chief Executive of the DLG (Steve Orr), stating that ‘I totally support the Mayor and Council management in immediately bringing this predicament to your attention, and through you to the Minister, and additionally I recommend on to the Premier’ (Wise, 2013). Mr Wise also wrote that delegates should be given the opportunity to ‘seek an external funding commitment to supplement the budget’. Mr Wise concluded his ‘Urgent Report’ with the following observations:

“Council’s primary problem is a liquidity problem, with Council having no control over generation of any sizeable income, and extremely limited abilities in cutting costs without cutting essential services. I suspect we are seeing at Central Darling Council the tip of the iceberg of the ongoing imposts, demands and expectations placed on all Councils (including cost shifting and one size fits all requirements) in a situation where there is extremely limited ability to absorb such externalities” (Wise, 2013).

September 2013. A delegation from the Shire attended the regional cabinet meeting in Broken Hill and stated ‘council’s financial position was perilous’ (Department of Premier and Cabinet, 2014, p. 57).

4 November 2013. Mayor Ray Longfellow wrote to ‘Local Member, seeking, among other things, an immediate cash injection of \$2 million for Central Darling Shire from the State Government’ (OLG, 2014, p. 5).

14 November 2013. Minister for Local Government wrote to the Shire requesting further information on its financial predicament (Longfellow, 2013).

22 November 2013. Mayor Longfellow responded to the correspondence from the Minister, stating that ‘Council strongly urges the State Government to support the equitable distribution of the FAGS ... the current contribution is insufficient to provide Council with the funds for servicing the basic needs of our communities’. In particular the

Mayor called for a ‘redistribution of FAGs (for the 2014/15 financial year) to provide an equitable and viable share for Central Darling’ (Longfellow, 2013).

23 December 2013. The Minister for Local Government appointed Mr Greg Wright (former General Manager of Camden Council) as Interim Administrator for three months.

March 2014. Minister for Local Government extended the period of Administration for a further three months.

14 March 2014. Report by consultants RSM Bird Cameron (commissioned by the OLG) was published. The desktop analysis stated that ‘it does not make sense for Council to conduct non-core activities, particularly where these are loss making’. Such activities included a Westpac banking agency, Post Office, aerodromes, swimming pools, community busses and aged care facilities. RSM Bird Cameron did not acknowledge that the council conducts the activities in response to market failure or cost shifting. For instance, the Post Office was taken on by the Shire after it entered into receivership and the ownership and maintenance obligations for the aerodromes were cost-shifted to local government from the Commonwealth (ALGA, 2015). Moreover, the airports are operated principally for the benefit of the Royal Flying Doctor Service, Rural Fire Service and State Emergency Service. It is therefore somewhat surprising that the consultant report recommended ‘either cessation or scaling back of ‘non-core activities’ that have been taken on by Council’ (RSM Bird Cameron, 2014, p. 13).

June 2014. Interim Administrator’s Report outlined a ‘recovery plan’ for the Shire. This included ‘returning’ two of the three community transport contracts to TransportNSW, ensuring all non-core services are fully funded, seeking a third party to operate the swimming pools, refusing RMS contracts which are not fully funded and ‘work[ing] constructively with LGNSW, the Grants Commission and other appropriate stakeholders to have the Financial Assistance Grants formula revised to better meet the needs of rural and remote Councils’ (Wright, 2014, p.14). The Interim Administrator’s Report concluded with the following sobering assessment of the Shire’s recovery:

“The issues facing the Central Darling Shire Council are serious and complex and they will take some considerable time to resolve. Indeed, I am not certain that the resolution of all the issues and the attainment of long term sustainability for the Council will – ultimately – be something that the community will be prepared to accept. The long-term solutions involve substantially pared back services and, in all probability, fewer jobs at the Council. The alternative, however, would be more unpalatable still.”

The final step into long-term suspension of the democratically elected body was the Public Inquiry conducted by Commissioner Colley and assisted by Angus Broad. We now turn our attention to this.

5. PUBLIC INQUIRY

On Tuesday 12 August 2014, Commissioner Richard Colley opened the Central Darling Shire Public Inquiry pursuant to s438(U) of the Local Government Act 1993. The Commissioner went to considerable pains to contrast the ‘rules’ of the inquiry to those which might operate in a regular court. In particular, the Commissioner noted that ‘the mere fact that a critical comment is made during the hearings or contained in the report of the inquiry is not of itself sufficient to open up that comment to scrutiny on the grounds of denial of procedural fairness’ and that the ‘findings cannot be impugned for want of procedural fairness no matter how distressing the criticism or condemnation might be to the individual concerned’ (Department of Premier and Cabinet, 2014, p. 3). The Commissioner also made reference to the RSM Bird Cameron report, before noting that ‘it is not intended to call any of its authors to appear at the public hearings’. Finally, the Commissioner noted that the purpose of the hearings was to allow him to make recommendations to the Minister, but emphasised that the Minister and Governor would be responsible for decision making.

Conflict of Interest?

Given the claims of inequitable FAG allocations made by the Mayor (Longfellow, November 2013) and Interim Administrator (Wright, June 2014), along with the direct involvement of the Deputy Chair of the NSWLGGC (May 2013) in the events preceding the Administration, it is somewhat surprising that Richard Colley – incumbent Chair of the NSWLGGC – was appointed by the Minister for Local Government as

Commissioner for the Public Inquiry. Indeed, Mr Colley's background has led some to question whether the Inquiry was conducted in accordance with the rules of procedural fairness, given that there may have been some grounds for a reasonable apprehension of bias. 'Actual bias or a reasonable apprehension of bias on the part of the decision maker are a breach of the rules of procedural fairness' (Butt, 2004, p. 49).

Richard Colley disclosed his position as Chair of the NSWLGGC well into the proceedings (after the luncheon adjournment on Wednesday 13 August, 2014) in the following exchange captured in the transcript of proceedings (but not in the Commissioner's Report), when he interjected to correct a witness who had incorrectly stated that FAG were tied grants:

COMMISSIONER. I probably should declare a – not an interest, but a – what would you call it?

MR BROAD: Defactive (*sic*) background.

COMMISSIONER: I happen to be the Chair of the New South Wales Grants Commission (Department of Premier and Cabinet, 2014, p. 116).

The exchange suggests that (i) the Commissioner recognised that his position as Chair of the NSWLGGC provided him with specialised knowledge relevant to the Public Inquiry and (ii) that the Commissioner was at pains to avoid the term '[conflict of] interest'.

Evidence on FAG Allocations

Councillor Rhoades, President of the NSW Local Government peak body (LGNSW), provided evidence to the Inquiry on its first day of hearings. Councillor Rhoades spent some time on the matter of inadequate FAG allocations and stated that:

"Councils such as Central Darling and many others should be receiving a greater share of that federal money than the way that the formula is used a lot of the times based on population" (Department of Premier and Cabinet, 2014, p. 20).

Moreover, Councillor Rhoades emphasised that the fiscal predicament of the Shire was not an isolated case:

“Yes this may have been the first of the pins to fall but that’s not to say there’s other pins that may not fall as well if certain things within the structure of Local Government in New South Wales don’t change” (Department of Premier and Cabinet, 2014, p. 22).

On the second day of hearings the matter of FAG allocations was raised by Jennifer Thwaites, Acting CEO of the Wilcannia Local Aboriginal Land Council. Her early comments cut right to the heart of the HFE principle:

“I would also argue very strongly in the equity areas that the services covered by this council that are being looked at as being non-essential, or essential services that have been cut back, go through the list, waste removal, water, sewerage, service centres, swimming pools, community busses, air strips or aerodromes used for the Royal Flying Doctor, post offices, aged care and community housing, property management, waste tips, cemeteries, animal registration, environmental planning, they are essential services and the residents of this Shire have the right to expect adequate service provision in those areas. Certainly we’re never going to match the service provision of the bigger urban areas, but why should we be penalised because we are living in a council area that is huge but has limited population and a socio-economically disadvantaged population” (Department of Premier and Cabinet, 2014, p. 116)?

It is a claim that the residents of Central Darling were not ‘able to function, by reasonable effort, at a standard not lower than the average standard of other local governing bodies in the state’ (Local Government (Financial Assistance) Act 1995, s6(3)(a)). Ms Thwaites then went on to assert that the NSWLGGC were not allocating grants equitably, and this led to the Commissioner’s interjection and disclosure of a ‘defactive (*sic*) background’:

“Well I’m not saying I’m an expert in it, but I’ve certainly gone through the guidelines for the federal assistance grants. The two highest priorities of that are socioeconomic disadvantage and Aboriginality. This Shire obviously, as the second highest socioeconomically disadvantaged community in NSW, and with an, I believe Aboriginal population of somewhere between 55 and 60 per cent, has to qualify with both of those ...” (Department of Premier and Cabinet, 2014, p. 116).

Councillor Page also spent some time expounding on what he perceived to be inadequate FAG:

“I have lobbied the Federal Government in regards to the funding, the FAGs grant, I met with Joyce Wheatley 15 years ago, she was the Chair of the FAGs committee, that the FAGs committee was not giving the councils in the outback the funding that it should have been getting ...” (Department of Premier and Cabinet, 2014, p. 154).

Councillor Page also provided a succinct summary of the relationship between adequate FAG and the sustainability of regions:

“I think, you know, councillors do have a good intent to make things better for their community so we need to have lobby groups lobbying so we have more funding coming in from FAGs, but at the same time, yes, we do need to have some housekeeping done as well ... it’s talking about the long term survival of outback Shires and councils and a lot of young people living in the outback now need to be given that bit of encouragement that things will get better in the future” (Department of Premier and Cabinet, 2014, p. 170).

A number of other witnesses also commented on FAG allocations (see, for instance, Councillor Astill’s evidence in Department of Premier and Cabinet, 2014). It is therefore somewhat surprising that the Commissioner’s 102-page report makes just the one reference to equity in FAG allocations and, in doing so, draws not on the evidence provided at the Inquiry, but rather on a selected text from the Interim Administrators Report:

“Equity in the financial assistance grants system would be beneficial, but is not the panacea for council's ills. The real and pragmatic answer is to cut costs” (Colley, 2014, p. 94).

Reduction in Services

Reduction in ‘non-core’ services advanced in the RSM Bird Cameron and Interim Administrator Reports had started to take place at the time of the Inquiry. For example, the community bus contracts had already been returned to TransportNSW and significant cuts to staffing had been executed (full-time equivalent staff had been reduced by almost one-fifth, from 54 in 2011/12 down to just 45 in 2013/14) (OLG, 2015).

The other strategy employed by the Interim Administrator to reduce the size of the overdraft facility (which had peaked at well over \$3 million) was to defer maintenance expenditure. The implications of this strategy were recognised by Councillor Sullivan:

“The council, if it stays like it is under its current structure, the recovery plan will only postpone the inevitable ... You’re not doing the workforce re-employments, you’re not replacing the housing, you’re not doing any work on the housing, you’re not replacing plant and equipment right. So if you don’t replace those you don’t spend the cash on them, you hold the cash in hand, right but somewhere along the line those things have to be fixed” (Department of Premier and Cabinet, 2014, p. 95).

The association between cuts in municipal staffing and services on the one hand, and the flow-on economic implications for the town on the other, was made by Councillor Page:

“If you do make cuts it affects your employment in the town, it affects the morale of the town. You need to look at both sides of it. Yes, we could be financially viable if [we only did] roads rates and rubbish, but if you look at the other side of it, what would be the overall outcome and the results, it's not an easy option to take” (Colley, 2014, p. 94).

This apparent reticence of Councillors (see also Looney in Department of Premier and Cabinet, 2014, p. 152) to accept cuts to services was cited by the Commissioner in his concluding remarks as justification for his recommendation to suspend the council until September 2020:

“It is difficult to see the current Council having the capacity to do so [implement the Recovery Plan], let alone, establishing a foundation for a sustainable future.”

The Role of HFE in Central Darlings Shire Liquidity Crisis

The principle of HFE which underpins the FAG grants rests on two key concepts:

- (i) The need for councils to exert reasonable revenue effort
- (ii) The normative proposition that all councils exerting reasonable revenue effort in the country should have the same potential in providing an average standard of services.

As established in Section 2, Central Darling Shire has the highest residential revenue effort in the state. Therefore, it is reasonable to assume that the first principle has been satisfied. The question then hinges on whether the FAG provided to Central Darling Shire are sufficient for it to provide the average of the standard of services provided in the state. This is highly questionable. For instance, 1 541km (or 96%) of the Shire’s roads are unsealed. Cuts have been made to swimming pool opening hours. The Shire does not have a library. Aerodromes provided for the benefit of the Royal Flying Doctor service are considered ‘non-essential’, as are cemetery facilities. Only one of the four principal towns making up the Shire has sewerage. White Cliffs does not have garbage collection but residents are required to cart their rubbish to the tip and *volunteers* attend to the management of the tip (RSM Bird Cameron, 2014). It is very difficult to argue that the residents at Central Darling Shire receive the standard level of services provided to other citizens of NSW.

Thus, there is *prima facie* evidence to suggest that the FAG allocation for Central Darling Shire was inadequate according to the HFE principles embodied in the enabling legislation. Moreover, since the period of Administration the Shire has been the beneficiary of some rather large increases to FAG allocations (see Table 4). In particular, the NSWLGGC Report on FAG allocations presented by Richard Colley (in his capacity as Chair of NSWLGGC) dated October 2014 – the same month as the Commissioner’s Report on the Public Inquiry – increases the total FAG

allocation for the Shire by just over 7 per cent during a period in which the state allocation actually decreased marginally (due to the Commonwealth freezing indexation of FAGs for a period of three years). One may question whether the Interim Administrator's report or the evidence heard at the Public Inquiry influenced this significant increase in FAGs. One must also question whether the additional \$815 256 p.a. received in grants from 2012/13 levels might have avoided the unprecedented liquidity crisis faced by the Shire on 4 November 2013.

Table 4. Changes to Financial Assistance Grant Allocations to Central Darling Shire, 2013–2015.

Period	General Purpose Component	Road Component	Total FAG
2012/13	\$2 200 748	\$1 409 193	\$3 609 941
2013/14	\$2 645 837	\$1 478 181	\$4 124 018
2014/15	\$2 944 280	\$1 480 917	\$4 425 197

Source: NSW Local Government Grants Commission (2014).

6. CONCLUDING REMARKS

It is interesting to contrast the flurry of media and scholarly attention engendered by the bankruptcy of the Municipality of Detroit in July 2013 with the dearth of analysis associated with the liquidity crisis experienced by Central Darling Shire at around the same time (see, for instance, Davey and Walsh, 2013; Stiglitz, 2013; Chung, 2014). One important reason for this disparity is the operation of an active municipal bond market in the United States (for varying accounts of the operation of the municipal bond market in the U.S., see, for example, Doty, 2012; Feldstein and Fabozzi, 2008; Johnson *et al.*, 2014). However, it is also clear that the remote location of the Shire may explain why so little attention has been given to Australia's first example of local government financial failure.

Horizontal Fiscal Equalisation grants are an essential component of a strong federation and play an important part in ensuring sustainable futures for communities in rural and remote regions. However, it is clear from the preceding analysis that the existing FAG allocations have not achieved the objectives enshrined in statute. Key recommendations to ensure FAGs achieve HFE objectives include: (i) changes to legislation to remove the stipulation for a minimum quantum based on population size and (ii) changes to NSWLGGC algorithms to remedy identified

deficiencies. There is evidence that a number of other rural and remote councils are experiencing acute fiscal distress. It is thus very important that prompt attention is given to implementing changes to FAG legislation and allocation practices.

A second outcome of this study is that it has cast light on some unsatisfactory processes leading up to the extraordinarily long period of Administration for Central Darling Shire. Suspension of democratically elected representatives for lengthy periods is an action of the utmost gravity. It is therefore reasonable to expect procedural fairness, thorough investigation and complete transparency. In particular, there should be no cause for the suggestion of apprehended bias. Moreover, it seems reasonable to expect that claims regarding the cause of Central Darling's financial predicament might have been investigated thoroughly in a manner akin to this study. It also seems reasonable to expect that reports arising from Public Inquiries might be responsive to the evidence recorded in the transcripts of proceedings.

For the residents of Central Darling Shire, Administration has meant significant cuts to services, employment and the level of maintenance expended on critical transport infrastructure. This serves to underline the importance of the aforementioned recommendations if we are to ensure that rural and remote communities might enjoy sustainable futures.

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